

Office of Chief Counsel
Internal Revenue Service

memorandum

CC:LM:5:SF:2:POSTF:114945-02
PKWebb

date: March 20, 2002 (amended version)

to: Internal Revenue Service
Large and Mid-Size Business Division
Attn: [REDACTED]
[REDACTED]

from: Paul K. Webb, Attorney (LMSB: Area 5)

subject: **Restricted Consents to Extend the Statute of Limitations**
Form 872-A: [REDACTED] Incorporated and Subsidiaries
Form 872-A: [REDACTED]

DISCLOSURE STATEMENT

This advice constitutes return information subject to I.R.C. § 6103.¹ This advice may also contain confidential information subject to attorney-client and deliberative process privileges and if prepared in contemplation of litigation, may be subject to the attorney work product privilege. Accordingly, any recipient of this document, including Examination or Appeals, may provide it only to those persons whose official tax administration duties with respect to this case require such disclosure. In no event may this document be provided to Examination, Appeals, or other persons beyond those specifically indicated in this statement. This document may not be disclosed to the taxpayer or its representatives.

This is an amended memorandum. Please destroy all copies of this memorandum dated prior to the above-listed date. This amended memorandum correctly states that the disputed issue (described below) exists for the fiscal years ending 1/31/[REDACTED] thru 1/31/[REDACTED]. Prior versions of this memorandum incorrectly included the fiscal year ending 1/31/[REDACTED] in this category.

Per your request of March 4, 2002, we have reviewed your proposed, restrictive language for the Forms 872-A for [REDACTED]

¹All citations herein are to Title 26, the Internal Revenue Code, unless otherwise specifically stated.

Incorporated and Subsidiaries consolidated group and for [REDACTED] International Limited. This memorandum sets forth our analysis of the proposed language, raises certain additional issues and makes general recommendations in regards to the Forms 872-A.

This advice relies on facts provided by you to our office. If you find that any of the stated facts are incorrect, please advise us immediately so that we may modify and correct this advice. This advice is subject to 10 day post-review by the Office of Chief Counsel. Please do not act upon this advice until we notify you of the results of that review.

Issues

1. Whether the below-quoted language for use on the [REDACTED] consolidated group Form 872-A adequately extends the statute of limitations for assessment of tax, restricted to the disputed foreign sales corporation commission issue.
2. Whether the below-quoted language for use on the [REDACTED] Form 872-A adequately extends the statute of limitations for assessment of tax and/or refund, restricted to the amount of foreign trade gross receipts properly reported.
3. How should [REDACTED] Incorporated's name, as parent of the consolidated group, be reflected on the Form 872-A.
4. Whether [REDACTED] Vice President of the Tax Department for [REDACTED] Incorporated, has the authority to sign the Form 872-A on behalf of [REDACTED] Incorporated.
5. Who should sign the Form 872-A for [REDACTED] [REDACTED], a foreign sales corporation incorporated under the laws of [REDACTED].

Summary Answers

1. The proposed language effectively extends the statute of limitations for assessment, limited to the foreign sales corporation commission disputed issue.
2. The proposed language effectively extends the statute of limitations for assessment, limited to the amount of foreign trade gross receipts.
3. The "Taxpayer" section of the respective Form 872-A should list "[REDACTED] Incorporated," rather than "[REDACTED] Incorporated and Subsidiaries." [REDACTED] Incorporated is

acting alone as agent for the consolidated group. We provide additional language for use on the Form 872-A that describes [REDACTED] Incorporated's role as agent for the consolidated group.

4. Based upon the "Officer's Certificate," we conclude that [REDACTED] has apparent authority to execute the Form 872-A on behalf of [REDACTED] Incorporated. Delaware law controls the ultimate disposition of authority, as [REDACTED] Incorporated is a Delaware corporation.
5. We recommend that you have one of the following corporate officers of [REDACTED] execute the respective Form 872-A on behalf of that corporation: (i) the chairman, deputy chairman, president or vice president of the board of directors; (ii) the managing director, the general manager, the comptroller, the secretary or the treasurer; or (iii) any other person who performs for the body corporate functions similar to those normally performed by the holder of any office specified above. [REDACTED] law controls whether or not the particular signatory has such authority. We note, however, that proper execution of this Form 872-A is solely in the taxpayer's interest as the purpose of the extension is to allow for a possible refund, pending resolution of the below-described disputed issue.

Facts

The Internal Revenue Service ("Service") is currently auditing [REDACTED] Incorporated ("[REDACTED]"). [REDACTED] is incorporated in the state of Delaware. [REDACTED] files its Federal tax returns using a fiscal year ending 1/31/XXXX. For its taxable years ending 1/31/[REDACTED] through 1/31/[REDACTED] (the "audited years"), [REDACTED] filed consolidated Federal tax returns with a group of subsidiary corporations. [REDACTED] is the parent of the consolidated group for all of the years covered in this memorandum. [REDACTED], the parent, has not changed its corporate identity or its name during the covered years.

[REDACTED] is involved the software industry. [REDACTED] produces various software products for sale worldwide. [REDACTED] utilizes a wholly owned foreign sales corporation ("FSC") by the name of [REDACTED] ("[REDACTED] FSC") to distribute software internationally. [REDACTED] and [REDACTED] FSC

██████████ FSC is a corporation organized under the laws of ██████████. ██████████ FSC is not part of the consolidated group of subsidiaries with which ██████████ files consolidated returns. See I.R.C. § 1504(a)(1), (b)(3) (foreign corporations are not "includible corporations" for consolidated return purposes). ██████████ FSC files Forms 1120-FSC using a fiscal year ending 1/31/XXXX.

██████████, ██████████ FSC and the Service would like to postpone resolution of their dispute until the appeal of Microsoft v. Commissioner, 115 T.C. 228 (2000) is finally decided. ██████████ and the Service previously entered into a restricted Special Consent to Extend Time to Assess Tax, Form 872-A, for the taxable years ██████████ through ██████████. ██████████ FSC similarly entered into a restricted Form 872-A to extend time for assessment of tax for the taxable years ██████████ through ██████████. ██████████, ██████████ FSC and the Service would like to enter into similar agreements for taxable years ██████████ and ██████████.

The Service's audit team inquires whether the following proposed restrictive language, used on the [REDACTED] Form 872-A for taxable years [REDACTED] through [REDACTED], is sufficient for use on the Form 872-A for taxable years [REDACTED] and [REDACTED]:

²Section 954 and related foreign sales corporation provisions were repealed, applicable generally to transactions after September 30, 2000. See P.L. 106-519, § 2.

[REDACTED]

Additionally, the Service's audit team inquires whether the following restrictive language, used on [REDACTED] FSC's Form 872-A for taxable years [REDACTED] through [REDACTED], is sufficient for use on the [REDACTED] FSC Form 872-A for taxable years [REDACTED] and [REDACTED]:

[REDACTED]

Our analysis of the proposed language, and other related observations, are set forth below.

According to the Service's audit team, the disputed issue will not result in any partnership adjustments to partnerships in which [REDACTED] or its subsidiaries are partners. According to [REDACTED], it was not involved in any partnerships during the covered period. Additionally, [REDACTED] FSC is purportedly [REDACTED]'s only foreign sales corporation.

Analysis

I. Effectiveness of the Forms 872-A in Extending the Statute of Limitations for the Disputed Issue.

As a general rule, Section 6501(a) provides a three year statute of limitations for assessing tax. Section 6501(c)(4) provides that the statute of limitations for assessment can be extended by written agreement between a taxpayer and the Service.

The Service utilizes Form 872-A to extend the statute of limitations for assessment to a date not more than 90 days after either (1) the Service mails Form 872-T to the taxpayer, or (2) the Service receives Form 872-T from the taxpayer. Issuance of a notice of deficiency supercedes a Form 872-A extension. Forms 872-A may also be used to restrict the extension of the statute of limitations to a specified issue or area of issues. See I.R.M. 25.6.22.8.

Form 872-A consents are not contracts. Stange v. United States, 282 U.S. 270 (1931). They are, however, unilateral waivers of a defense by the taxpayer. Grunwald v. Commissioner, 86 T.C. 85, 89 (1986); Piarulle v. Commissioner, 80 T.C. 1035,

1042 (1983). Because Section 6501(c) requires the consent to be a written agreement, contract principles are significant in interpreting and applying the law as to such agreements. Piarulle v. Commissioner, 80 T.C. at 1042. This is important because ambiguities in the terms of a consent, like a contract, are generally construed against the drafter. See Ripley v. Commissioner, 103 F.3d 332 (4th Cir. 1996); Anthony v. United States, 987 F.2d 670, 673-74 (10th Cir. 1993); Roszkos v. Commissioner, 850 F.2d 514, 516-17 (9th Cir. 1988), cert. denied, 489 U.S. 1012 (1989).

Extreme care should be taken in writing restrictive language in a consent. I.R.M. 25.6.22.8.11. The restriction should not foreclose utilization of alternative rationale in making the adjustment, if such action becomes necessary. I.R.M. 25.6.22.8.11.(1). Thus, the restrictive language should describe the area or areas of consideration rather than the proposed tax treatment. I.R.M. 25.6.22.8.11.(1).a. Code sections should not be included in the restrictive language. I.R.M. 25.6.22.8.11.(1).b.

Each restricted consent must contain a basic restrictive statement and a description of the area(s) of consideration. While the area(s) of consideration will vary with each restricted consent, the Internal Revenue Manual suggests the following basic restrictive statement:

The amount of any deficiency assessment is to be limited to that resulting from any adjustment to (description of the area(s) of consideration) including any consequential changes to other items based on such adjustment.

I.R.M. 25.6.22.8.12.

Area Counsel must approve the legal sufficiency of any restrictive language prior to soliciting a restricted consent. I.R.M. 25.6.22.8.6. We separately reviewed the proposed Form 872-A restrictive language for [REDACTED] and [REDACTED] FSC.

A. The [REDACTED] 872-A Restrictive Language.

The proposed restrictive language states that the "[REDACTED]

[REDACTED]

[REDACTED]."

Under the former and applicable FSC provisions, a large portion of a FSC's "foreign trade income" is treated as foreign source income not effectively connected with a trade or business conducted in the U.S., thus permanently escaping U.S. taxation. See I.R.C. §§ 921(a) and 923(a). When a "commission FSC" (rather than a "buy-sell" FSC) facilitates qualifying export transactions, the commission income the FSC receives from its U.S. principal constitutes foreign trade income. Whether the commission income a FSC receives constitutes foreign trade income depends on the presence of qualifying export transactions that give rise to "foreign trading gross receipts" ("FTGRs"). I.R.C. § 923(b). Transactions give rise to FTGRs if they involve the sale, lease, or license of "export property." I.R.C. § 924(a).

Qualifying "export property" transactions that generate FTGRs permit a U.S. principal to invoke administrative pricing rules to compute a deductible FSC commission expense. I.R.C. § 925(b); Treas. Reg. §§ 1.925(a)-1T(b)(1), (b)(2)(ii), and (d)(2). The larger the FSC commission the U.S. principal pays and deducts, the greater the portion of profits from export transactions that permanently escapes U.S. taxation. This is true because the U.S. principal deducts the commission expense, whereas the related FSC need only report a portion of the received amount as U.S. taxable income. See e.g., Microsoft v. Commissioner, 115 T.C. 228 (2000).

As in Microsoft v. Commissioner, 115 T.C. 228 (2000), the Service asserts that the royalties accrued from [REDACTED] FSC export licensing transactions were not FTGRs because they did not arise from transactions in "export property." As a consequence, if the Service's position prevails, [REDACTED]'s claimed deduction for FSC commission expenses will be reduced.

Given the above, we believe the proposed language in the Form 872-A adequately incorporates future adjustments to [REDACTED]'s claimed FSC commission expenses and any consequential changes to other items on the consolidated return. The proposed Form 872-A language is both sufficiently detailed as to identify the issue covered and sufficiently broad so that the disputed issue, and related adjustments, can be determined and assessed upon ultimate resolution of the issue.

B. The [REDACTED] FSC 872-A Restrictive Language.

FSCs are, by definition, corporations organized pursuant to the laws of a qualified foreign country or U.S. possession. I.R.C. § 922(a)(1)(A). In general, the corporate existence of a FSC is respected for U.S. tax purposes, including periods of

limitation. See generally, Union Carbide Corp. v. Commissioner, 110 T.C. 375 (1998).

Because a FSC is organized under the laws of a foreign country or a U.S. possession, it cannot be part of its U.S. parent's consolidated group. See I.R.C. §§ 922(a)(1)(A); 1504(a)(1),(b)(3). Thus, the Service is appropriately securing a separate statute extension from [REDACTED] FSC.

The proposed language for the [REDACTED] FSC consent extends the statute of limitations for deficiency assessment or refund, limited to "[REDACTED]
[REDACTED]
[REDACTED]."

Because the amount of income reported by a FSC is directly related to the amount of income reported by its U.S. supplier, a FSC redetermination and likewise a commission redetermination, effects the other party, i.e., either the U.S. supplier or the FSC. The disputed issue in this case involves whether or not the royalties qualify as FTGRs. If not, [REDACTED]'s commission deduction will be substantially reduced and [REDACTED] FSC's taxable income will similarly be reduced. Assuming the Service prevails, the end result will be a tax deficiency owing by [REDACTED], with a significantly smaller refund due owing to [REDACTED] FSC.

Given the above, we conclude that the proposed language for the Form 872-A for [REDACTED] FSC adequately incorporates and addresses the disputed issue. Any adjustments made by the Service to [REDACTED] FSC's Form 1120-FSC will be in relation to the amount of qualifying FTGRs. As stated above, the FTGRs adjustment will effect FSC's foreign trade income. The proposed Form 872-A language is both sufficiently detailed as to identify the issue covered and sufficiently broad so that the disputed issue, and related adjustments, can be determined and assessed upon ultimate resolution of the issue. Finally, to place the [REDACTED] FSC consent in proper context, we note that it is being executed solely for the purpose of generating a refund for [REDACTED] FSC in the event that the Service ultimately prevails in the disputed issue.

II. Sufficiency of the Forms 872-A as to Taxpayer Identification and Signature of the Respective Agents.

In reviewing [REDACTED]'s prior Forms 872-A for taxable years [REDACTED] through [REDACTED], we note a few changes that should be made when executing the Form 872-A for taxable years [REDACTED] and [REDACTED]. We

additionally provide some general, instructive analysis as to executing Form 872-A.

A. The Taxpayer Identification Section: [REDACTED] 872-A.

The "taxpayer" on the prior Form 872-A is identified as "[REDACTED] Incorporated and Subsidiaries." [REDACTED]'s EIN is listed on the Form 872-A.

The governing regulations provide that "The common parent . . . shall be the sole agent for each subsidiary in the group, duly authorized to act in its own name in all matters relating to the tax liability for the consolidated return year." Treas. Reg. § 1.1502-77 (emphasis added).

In the present situation, [REDACTED] is the common parent for the consolidated group with which it filed consolidated Federal tax returns for the audited taxable years. As such, [REDACTED] is the sole agent for the group for all matters relating to the income tax liability for the consolidated return years. See Treas. Reg. § 1.502-77(a). [REDACTED] is duly authorized under the regulation to act in its own name on behalf of the consolidated group. See Treas. Reg. § 1.502-77(a). Thus, inclusion of the "and Subsidiaries" language in the taxpayer identification section of the Form 872-A is unnecessary (and technically incorrect) surplusage. However, this technical defect has no effect on the enforceability of the Form 872-A.

In securing the Form 872-A for taxable years [REDACTED] and [REDACTED] we recommend that you type an asterisk next to the taxpayer's name ("[REDACTED] Incorporated") in the caption section. Then, at the bottom of the form, type another asterisk and insert the following text:

This is with regard to the consolidated tax liability of the [REDACTED] Incorporated and Subsidiaries consolidated group for the group's tax years ending January 31, [REDACTED] and January 31, [REDACTED].

By completing the form in this suggested manner, the parent, as sole agent for the group, is properly identified as "[REDACTED] Incorporated" and the form adequately explains that the parent is acting on behalf of the consolidated group as to the consolidated group's tax liability.

B. The Signature Section.

1. Whether [REDACTED] Vice President of the Tax Department for [REDACTED] has Authority to Execute the Form 872-A for [REDACTED].

The signature line on the prior Form 872-A for taxable years [REDACTED] through [REDACTED] sets forth the signature of [REDACTED] General Counsel and Secretary. According to the information you provided, [REDACTED], Vice President of the Tax Department for [REDACTED], will sign the Form 872-A on behalf of [REDACTED] for the taxable years [REDACTED] and [REDACTED].

In response to Field Counsel's inquiry, the audit team provided a document entitled "Officer's Certificate." Said document states:

I hereby certify that I am the duly elected and acting Senior Vice President Business Development, General Counsel and Secretary of [REDACTED] Inc., a Delaware corporation (the "Company").

As of the date hereof, [REDACTED] is the duly elected and acting Vice President, Tax of the Company and, pursuant to the Bylaws of the Company and authority delegated by the Board of Directors of the Company, as an officer he has the authority to execute documents on behalf of the Company on all tax-related matters.

The document is thereafter signed and dated [REDACTED], by [REDACTED] as Senior Vice President, Business Development, General Counsel and Secretary.

Section 6061 provides that any return, statement, or document made under any internal revenue law must be signed in accordance with the applicable forms or regulations. I.R.C. § 6061. The regulations implementing Section 6501(c)(4) (agreements to extend the statute of limitations for assessment of tax) do not specify who may sign consents executed under that section. Accordingly, the Service generally applies the rules applicable to execution of original returns to consents to the extension of time to make an assessment. Section 6062 provides, generally, that a corporation's income tax returns must be signed by the president, vice-president, treasurer, assistant treasurer, chief accounting officer or any other officer duly authorized to act. The fact that an individual's name is signed on the return is

prima facie evidence that the individual is authorized to sign the return. Accordingly, any such officer may sign a consent, whether or not that person was the same individual who signed the return. See also, Rev. Rul. 83-41, 1983-1 C.B. 349, clarified and modified by Rev. Rul. 84-165, 1984-2 C.B. 305.

For domestic corporations, the state law for the state of incorporation controls when there are questions as to the authority of a signatory. [REDACTED] is a Delaware corporation. Delaware corporate law provides that the bylaws and board resolutions not inconsistent with the bylaws dictate the assignment of duties and responsibilities for corporate officers. See 8 Del. C. §§ 141, 142. Generally, under Delaware law, corporate officers are the agents of the corporation for acts undertaken in the regular or ordinary course of business and can bind the corporation within the scope of their actual or apparent authority. See Hessler, Inc. v. Farrell, 226 A.2d 708 (Del. 1967); Guyer v. Haveg Corp., 205 A.2d 176 (Del. Super. 1964), aff'd 211 A.2d 910 (Del. 1965);

Based upon the "Officer's Certificate" provided by [REDACTED] [REDACTED] is both an officer of [REDACTED] and has the apparent authority to execute documents on its behalf for "all tax-related matters." As such, we conclude that [REDACTED] has at least the apparent authority to execute the Form 872-A on behalf of [REDACTED]. However, as the "Officer's Certificate" is approximately eight months old, we recommend that you verify that it is still operative.

When securing the Form 872-A from [REDACTED], and in securing future statute extension forms, we recommend that you list the company for which the signatory works in the signature section, along with the company's TIN or EIN, so that the face of the form reflects the requisite authority, i.e., that the signatory has authority to act as an agent for the parent company. See I.R.M. 25.6.22.6.2(4). For example, the signature section of the Form 872-A might appear as follows:

CORPORATE NAME: [REDACTED] Incorporated

CORPORATE OFFICERS SIGN HERE: [REDACTED] Vice
President of Tax and officer of [REDACTED]
Incorporated, EIN: [REDACTED] Agent for
[REDACTED] Incorporated and Subsidiaries
consolidated group.

b. Who Should Sign the Form 872-A for [REDACTED] FSC.

[REDACTED] FSC is a foreign corporation organized under the laws of [REDACTED]. As such, the authority of an officer to consent to extend the period of limitations for assessment for [REDACTED] FSC must be determined under [REDACTED] law.

[REDACTED] law provides that:

[REDACTED]

[REDACTED].

Under [REDACTED] law, corporate "officers" are defined as:

[REDACTED]

[REDACTED].

It is our understanding of [REDACTED] law, that any of the above-listed officers of a [REDACTED] corporation can bind that corporation in ordinary business affairs. Therefore, we recommend that the Service's audit team verify that one of the above-listed officers of [REDACTED] FSC, the [REDACTED] corporation

(not [REDACTED] the parent), will execute the Form 872 on behalf of [REDACTED] FSC.³

III. I.R.M./Chief Counsel Outline.

Before securing the consent agreements, we recommend that you review the relevant Internal Revenue Manual provisions on statute extensions. See I.R.M. 25.6.22. Finally, please note that the Corporate division of the Office of Chief Counsel has developed an outline addressing extensions of the statute of limitations to assess tax in the context of taxpayers filing consolidated Federal tax returns. The outline is entitled "Consent to Extend the Time to Assess and Agent for a Consolidated Group." We believe this outline provides useful guidance for field agents who secure consents to extend the statute of limitations. The following link to the Chief Counsel's intranet web-page can be used to access a complete copy of the outline:

http://casecn01.irsccounsel.treas.gov/intranet_new/corp/tmaterials/Consents%20and%20Agent%20for%20Group%20outline.wpd

Conclusion

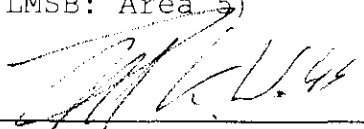
Conditioned upon the above suggestions, we conclude that execution of the proposed Forms 872-A will effectively extend the statute of limitations for assessment as to the disputed issue.

Please telephone attorney Paul K. Webb at (415)744-9217 if you have any questions regarding this memorandum.

³We understand that [REDACTED] FSC's statute of limitations is being extended for the sole purpose of issuing a refund to the taxpayer in the event that the Service ultimately prevails in the appeal of Microsoft v. Commissioner, 115 T.C. 228 (2000). Therefore, it is actually in the taxpayer's best interest to have an authorized officer execute the Form 872-A on its behalf.

This writing may contain privileged information. Any unauthorized disclosure of this writing may have an adverse effect on privileges, such as the attorney client privilege. If disclosure becomes necessary, please contact this office for our views.

LAUREL M. ROBINSON
Associate Area Counsel
(LMSB: Area 5)

By: 
PAUL K. WEBB
Attorney (LMSB: Area 5)

Attachments: as stated.

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